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UNCLAS SECTION 01 OF 04 MANILA 000998

SIPDIS

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STATE FOR EAP/MTS, EAP/EP, EEB/IFD/OMA  
STATE PASS EXIM, OPIC, AND USTR  
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AIT TAIPEI PASS TO KAOHSIUNG

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TAGS: EFIN ECON PREL PGOV KINR KCOR RP CM

SUBJECT: Limits of Chinese Soft Power in the Philippines

Ref: A) 2007 Manila 2456, B) Manila 668

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**¶1.** (SBU) Summary: China's soft-power diplomacy has recently stumbled in the Philippines under a months-long media barrage of corruption allegations and scandal investigations. This has occurred against the backdrop of a tenfold increase in bilateral trade since 2000, increased security cooperation, and the signing of dozens of bilateral agreements in recent years. In spite of the influence wielded by Filipinos of Chinese ancestry, recent scandals have reawakened long-held views among Filipinos that link ethnic Chinese to corrupt practices. Strengthened Philippine-PRC ties do not imply a weakening of our strong bonds with the Philippines. Polls show a majority of Filipinos view the U.S. as the Philippines' most trusted ally, both now and 10 years hence. The Mission continues to stress that we do not view increased Chinese trade, investment, and development assistance as detrimental, while noting the need to use aid to strengthen transparency and good governance. End summary.

Background of Chinese-Philippine Relations

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**¶2.** (U) Mainland Asia's relations with the Philippines long predate the arrival of Iberian influence in the 16th century. Trade with Mainland Asia, including China, was flourishing by the 10th Century, and by the time of the Ming Dynasty (1368-1644), many Chinese traders had settled in Manila and other trading centers throughout the Philippines and elsewhere in Southeast Asia. Chinese merchants later forged mutually beneficial alliances with the Hispanic elite who dominated political and religious life in the Philippines for over three centuries. Under the Spanish 'comprador system,' ethnic Chinese were allowed a monopoly on trade between the Philippines and China, a key leg in the fabulously lucrative 'galleon trade' between Manila and Europe via Acapulco, and allowed to dominate Philippine domestic businesses. However, the Hispanic elite also sought to keep the power of the Chinese in check through discriminatory laws and periodic bloody pogroms.

**¶3.** (SBU) Ethnic Chinese still enjoy disproportionate economic and political power in the Philippines; by one estimate, they comprise

only two percent of the nation's population, but control 50 percent of listed equities. Filipino-Chinese have made great strides in recent decades in overcoming the long-standing racial prejudices; nonetheless, there is still a latent sense among many Filipinos that the Chinese are amoral profiteers. The increasing economic and political influence of China in regional affairs has reawakened this broadly held stereotype and fed a suspicion that both Chinese development assistance and business practices are rife with corruption and intended to further Chinese -- not Filipino -- ends.

#### Growing Philippine-PRC Relations

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**¶4.** (SBU) Since reciprocal state visits by Philippine President Gloria Macapagal-Arroyo and PRC President Hu Jintao in late 2004 and early 2005, the Philippines has signed dozens of agreements with China on a wide range of economic, political, cultural, and military issues. In January 2008, the PRC Embassy in the Philippines announced that the trade volume between the Philippines and the Chinese mainland had surged to a record high of \$30.62 billion, an almost 10-fold increase from the \$3.14 billion in 2000. (We have questioned these figures in ref B. By comparison, trade between the U.S. and the Philippines was \$17.1 billion in 2007.)

**¶5.** (U) Defense cooperation between China and the Philippines expanded significantly during President Arroyo's state visit to China, as she and Premier Wen Jiabao identified key areas of cooperation, such as sea rescue, disaster mitigation, and training exchanges. Setting aside their competing territorial claims to the Spratlys, the two countries espoused the joint development of the disputed area. In November 2004, the Philippine Defense Secretary and his PRC counterpart signed a memorandum of understanding on defense cooperation in Beijing.

**¶6.** (U) In May 2007, high-ranking People's Liberation Army (PLA) and Philippine defense department officials held their third bilateral

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defense and security dialogue in Manila, during which they discussed counter-terrorism, the situation in Northeast Asia, and mutual concerns and interests related to maritime security, national defense, and military construction. At the end of the dialogue, the PRC delegation promised more security assistance to intensify defense relations between the PLA and the Armed Forces of the Philippines. On the Philippine side, defense officials reaffirmed Manila's adherence to the one-China policy and acknowledged China's important contribution to international and regional peace.

**¶7.** (U) Though China has also invested heavily in the Philippine agricultural and mining sectors, its most prominent economic activities in the Philippines are in infrastructure development. Beijing has poured \$450 million into the rehabilitation of the North Luzon Railway system, linking metropolitan Manila with Angeles City in central Luzon. The provision of a \$450 million soft loan for the rehabilitation project, in addition to US\$500 million in other soft loans (for the construction of a dam, an elevated highway, and a provincial airport), makes Beijing one of the biggest providers of concessionary loans to the Philippines. In 2007, Beijing indicated an interest in upgrading the Southern Luzon rail system as well.

#### Big Brother

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**¶8.** (SBU) In her opening statement at the 10th ASEAN-China Summit in January 2007 President Arroyo likened China to a "big brother" and called on Southeast Asian leaders to continue strengthening ties with the regional giant, saying Beijing has an important and strategic role in the economic development and security of the Asia-Pacific region. Philippine Trade Secretary Peter Favila and Finance Secretary Margarito Teves have both described the Philippines' growing trade with China as cushioning the impact of a U.S. economic slowdown.

Allegations of Corruption and Improper Influence

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**¶9.** (SBU) More recently, however, PRC-Philippine relations have hit a rough patch. As reported reftel, a \$329 million contract for a national broadband network signed by a Philippine Cabinet Secretary and China's state-owned ZTE Corporation in April 2007 unleashed allegations of corruption that received extensive media coverage in the Philippines. The number of senior officials tainted by this scandal continues to grow as lengthy Senate hearings implicated President Arroyo's husband Jose Miguel "Mike" Arroyo, various cabinet members, and prominent business people. While there is little hard evidence to support the allegations, politicians and media used a broad brush to tar all associated with the project.

Bungled Chinese Response

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**¶10.** (SBU) The ZTE case is typical of the deals that China reportedly uses worldwide to make friends and buy influence. Unlike the World Bank, the IMF, and many bilateral providers of assistance here, China does not link its aid to issues such as good governance, rule of law, or respect for human rights. Public skepticism and scrutiny have underlined shortcomings in China's soft power efforts. For months after the ZTE scandal surfaced, the PRC Embassy would only comment that scandal allegations were "purely domestic" or an "internal Philippine affair." In October 2007, Emboffs met with PRC Embassy officials who seemed to hint at questionable tactics, saying the PRC government believed "in following local laws, but also in following local traditions." However, non-Chinese contacts reported to us that the publicity given the ZTE scandal violated the Chinese diplomatic injunction to maintain a low profile. The resulting damage to China's image reportedly hastened the replacement of China's ambassador to the Philippines in September 2007.

Emotional Outburst Directed at Chinese

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**¶11.** (SBU) The ZTE scandal hearings before the Philippine Senate featured Senate Foreign Relations Committee Chair Miriam Santiago's

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emotional outburst that "the Chinese invented corruption for all human civilization." Although the PRC Embassy afterwards demanded and received an apology, Senator Santiago's statement reflected the widely held Filipino view that the Chinese frequently use unethical business practices. Interestingly, newspaper editorials have contrasted this perception of unethical Chinese with the Filipino perception of honest Americans, and have specifically praised the U.S. Foreign Corrupt Practices Act.

Ineffective Damage Control

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**¶12.** (SBU) The Arroyo administration formed a panel to review all Chinese government-funded projects in the Philippines, and put on hold the broadband project, a cyber education project, and two large agricultural projects. When Arroyo met Chinese President Hu Jintao in Shanghai October 2, 2007, she reportedly spent much of the meeting explaining her decision to cancel the ZTE contract and suspend other projects funded by China. Afterwards, President Arroyo urged China to increase its investments in the Philippine agriculture, fisheries, and infrastructure sectors, thanked it for providing loans for the North Luzon Railway project, and asked the PRC to conduct more joint exploration activities in the South China Sea to strengthen its partnership with ASEAN member states. However, despite the Arroyo administration's efforts to contain the damage, the spoken and whispered allegations of Chinese corruption expanded to cover virtually all major PRC-funded projects in the Philippines.

More Scandals

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**¶13.** (SBU) In mid-2007, it looked as though China had the inside track on winning the contract for the expansion of the airport at the former Clark airbase. However, allegations of overpricing and kickbacks in China-financed and -built infrastructure projects arguably led China to withdraw its offer of concessionary financing

for the project in order to avoid the controversy that might follow the contract. The scrutiny of Chinese-funded projects has intensified and expanded to cover the Bauang pump irrigation project, the General Santos Fish Port Complex, the Northrail Project, and others. Senate investigators have recently summoned Chinese ZTE executives for questioning.

And Then There's the Spratlys...

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¶14. (SBU) Controversy over the failed ZTE broadband deal even spilled over to affect the delicate status quo in the disputed Spratly Islands, where tensions over competing territorial claims were lowered by a 2005 trilateral agreement among the Philippines, China, and Vietnam that facilitated peaceful joint exploration of the islands' anticipated mineral resources. In the wake of the ZTE scandal, allegations emerged that the Arroyo administration allowed the seismic exploration deal in exchange for bribe-tainted loans. Legislative and media critics of Arroyo have suggested that the administration is dragging its feet in meeting a 2009 UN Convention on the Law of the Sea deadline for defining the Philippine archipelago's baselines.

Comment

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¶15. (SBU) China's use of soft power in the Philippines has given it another bruising lesson in the role of a free press and political opposition in a democracy. The current problems are likely a temporary setback for China and the Philippines, as bilateral trade and policy ties continue to rise in concert with the growth in China's economy and influence. Still, strengthened Philippine-PRC ties do not imply a weakening of traditionally strong Philippine bonds with the U.S. Public opinion polls consistently show that a majority of Filipinos sees the U.S. as the Philippines' most trusted ally and, when asked which country they see being most important to the Philippines in 10 years, a similar majority respond that it will be the United States. At the same time, we have made clear in both

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public and private comments we do not view increased Chinese trade, investment, and development assistance as detrimental, even while stressing the need to use aid to strengthen transparency and good governance.

Kenney